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In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 622

COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

ISADORE GOLONSKY AND FRANK GOLD

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgments of the United States Court of Appeals for the Third Circuit entered in these consolidated causes on November 28, 1952.

OPINIONS BELOW

The opinion of the Tax Court (R. 10–12) is reported in 16 T. C. 1450. The opinion of the Court of Appeals (R. 17–19) is reported in 200 F. 2d 72.

JURISDICTION

The judgments of the Court of Appeals were entered on November 28, 1952. (R. 20–21.) The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTION PRESENTED

Whether the sum of money received by the lessees of certain real property from the owner of the property for the accelerated termination of the lease constituted ordinary income to the lessees under Section 22 (a) of the Internal Revenue Code, or capital gain under Section 117 of the Code.

STATUTE INVOLVED

Internal Revenue Code:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> * * * * *
>
> (26 U. S. C. 1946 ed., Sec. 22.)
>
> SEC. 117. CAPITAL GAINS AND LOSSES.
>
> * * * * *
>
> (b) [As amended by Sec. 150 (c) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Percentage Taken Into Account.*—In the case of a taxpayer, other than a corpora-

tion, only the following percentages of the gain or loss recognized upon the sale or exchange of a capital asset shall be taken into account in computing net capital gain, net capital loss, and net income:

100 per centum if the capital asset has been held for not more than 6 months;

50 per centum if the capital asset has been held for more than 6 months.

* * * * *

(26 U. S. C. 1946 ed., Sec. 117.)

STATEMENT

The facts, as found by the Tax Court (R. 10–12), may be summarized as follows:

Taxpayer-lessee Golonsky leased the premises at 1842 Market Street, Philadelphia, for a term of one year from October 1, 1938, the term to continue from year to year unless terminated by a written notice given at least three months prior to the end of an annual term. Golonsky, with the consent of the lessor, assigned the lease on August 8, 1941, to himself and taxpayer Gold. (R. 10.)

Sansom Realty Company acquired title to the premises on June 1, 1944, subject to the lease. Notice to terminate the lease on September 30, 1944, was given by the lessor. Sansom Realty Company entered into a contract with the taxpayers dated June 13, 1944, whereby the taxpayers agreed to vacate the premises and terminate the lease on or before June 30, 1944, in consideration of the payment to them of the sum

of $7,500. The agreement was carried out in accordance with its terms and the taxpayers received the $7,500 in 1944. The taxpayers did not report the transaction on their returns for the year 1944. The Commissioner, in determining deficiencies in the taxpayers' income taxes for the year 1944, held that each taxpayer had received ordinary income of $3,750 from the transaction. (R. 10–11.)

The Tax Court, two judges dissenting, held that the amount received by each of the two taxpayers constituted capital gain rather than ordinary income, basing its conclusion on the ground that there was a sufficient transfer of property to bring the transaction within Section 117 of the Internal Revenue Code. (R. 10–12.) On petition for review filed by the Commissioner, the court below affirmed the decision of the Tax Court, holding that the cancellation transaction was a "sale" of a capital asset within the meaning of Section 117 of the Internal Revenue Code. (R. 17–19.)

REASONS FOR GRANTING THE WRIT

1. There is a substantial conflict between the decision of the court below in the present case and that of the Court of Appeals for the District of Columbia Circuit in *United Cigar-Whelan Stores Corp.* v. *District of Columbia,* 176 F. 2d 952. While the *United Cigar-Whelan* case arose under the District and not the general federal tax statute, the decision turned upon the same

question, namely, whether the cancellation of a lease in consideration of a sum of money paid by the lessors to the lessee was a "sale or exchange of a capital asset." The District of Columbia Revenue Act of 1939, c. 367, 53 Stat. 1085, 1091, Section 6 (47 District of Columbia Code (1940 ed.), Sec. 47.1506), provided in part—using terms identical with those in Section 117 of the Internal Revenue Code, *supra,* pp. 2–3—that gain or loss from "the sale or exchange of a capital asset" should not be recognized in the computation of net income. In that case, several years before the end of the lease, the lessors paid the lessee (the taxpayer) $30,000 to cancel the lease. Both the Board of Tax Appeals for the District of Columbia and the United States Court of Appeals for the District of Columbia Circuit held that the accelerated termination of the lease was not a sale or exchange within the meaning of the above-mentioned statute and that the gain should, therefore, be treated as ordinary income. In the case at bar, both the Tax Court and the court below held that the accelerated termination of the lease for a cash payment was a sale, and that the sum received by the lessee was taxable as a capital gain (R. 10–12, 17–19). The court below recognized that there was a substantial conflict between its decision and that of the Court of Appeals for the District of Columbia Circuit, stating (R. 19): "With due deference we disagree with the court in that case, as did the Tax Court here."

A review of the present case would therefore resolve this conflict.[1]

2. The decision below does not appear to be in harmony with *Hort* v. *Commissioner,* 313 U. S. 28. In that case a lessor received a lump sum payment from the lessee in consideration of the termination of the lease. The lessor (taxpayer in that case) contended before the Board of Tax

[1] The District of Columbia Revenue Act of 1939, 53 Stat. 1085, under which the *United Cigar-Whelan* case arose, was repealed by Section 1 of the District of Columbia Income and Franchise Act of 1947, 61 Stat. 328, 331, with appropriate saving provisions. Section 29 of the 1939 Act, 53 Stat. 1100; 47 D. C. Code (1940 ed.), Section 47–1529, required the assessor to "apply as far as practicable the administrative and judicial interpretations of the Federal income-tax law so that computations of income for purposes of this title shall be, as nearly as practicable, identical with the calculations required for Federal income-tax purposes." It does not appear, however, that Section 29 was a controlling factor in the *United Cigar-Whelan* case, since it was not mentioned by the court, and since it does not appear that, at the time of the decision, there were any published rulings under the Federal law which governed the issue. The only authority cited by the court was its own prior decision in *Hale* v. *Helvering*, 85 F. 2d 819, which related to the transfer of promissory notes. That case was clearly not dispositive of the question presented, and was not intended by the court to be so, since the court pointed to it merely as a comparison. Consequently, it is scarcely plausible that the repeal of Section 29 would cause the Court of Appeals for the District of Columbia Circuit to change its view on the question presented, particularly since the provisions of the 1947 Act which exclude from the definition of gross income gains from the "sale or exchange" of capital assets are couched in substantially identical language as those contained in Section 6 of the 1939 Act. Cf. 61 Stat. 336, Subsection B (11) with 53 Stat. 1091, Section 6.

Appeals that if the amount received was income, it was capital gain. The Board rejected the argument on the ground that there was not a "sale or exchange" of a capital asset, saying (39 B. T. A. 922, 926):

> Here the lease was extinguished, not sold or exchanged. * * * Neither business men nor lawyers refer to the cancellation or forfeiture of a lease for a consideration as a sale or exchange.

This Court also held that the amount so received by the lessor constituted ordinary income under Section 22 (a) of the Revenue Act of 1932, c. 209, 47 Stat. 169, and not capital gain under Section 101 of that Act.[2] It apparently assumed that the Board was correct in its conclusion that the extinguishment of the lease was not a "sale or exchange." If there was no "sale" in that case where the lessor received payment for the cancellation, it would seem to follow that there was likewise no sale where the lessee received payment, for in both cases the transaction otherwise is precisely the same, namely, the lease is terminated or extinguished, the lessee is relieved of his obligation further to pay rent, and possession of the property reverts to the lessor. The distinction between a "sale" of a lease to a third

[2] Section 22 (a) of this Act is substantially the same as Section 22 (a) of the Internal Revenue Code, *supra* (p. 2), and Section 101 of the 1932 Act corresponds in all respects material here to Section 117 of the Internal Revenue Code, *supra* (pp. 2–3).

party and a cancellation of a lease is no less substantial than the claimed distinction between a "sale" of a bond to a third party and payment and discharge of a bond. See *Fairbanks* v. *United States,* 306 U. S. 436. It would appear decisive that the cancellation of a lease, like the payment of a bond, is not a "sale or exchange" within the commonly accepted meaning of the words.

3. The question is a recurrent one. Payments to lessees for accelerated termination of leases are not unusual in the course of everyday business. A short time ago the Tax Court decided a similar question in favor of the taxpayer, citing the present decision. *McCue Bros. & Drummond, Inc.* v. *Commissioner,* 19 T. C. No. 84, promulgated January 21, 1953.

In a recent Tax Court decision, now on appeal to the Second Circuit, it was held that the termination, or modification, of a contract granting the taxpayer the exclusive right to sell a product in consideration of a cash payment was a sale, and that the sum so received by the taxpayer was taxable as a capital gain, not as ordinary income. *Starr Brothers, Inc.* v. *Commissioner,* 18 T. C. 149. In another Tax Court decision, now on appeal to the Fifth Circuit, it was held that money received by lessees from their lessor in consideration of striking a protective clause from the lease was derived from a "sale" within the meaning of Section 117 of the Internal Revenue

Code. *Ray* v. *Commissioner,* 18 T. C. 438. In both of these cases the Tax Court cited its decision in the present case, and both cases were cited in the opinion of the court below. (R. 19, note.)

CONCLUSION

For the reasons stated, the petition for a writ of certiorari should be granted.

Respectfully submitted.

WALTER J. CUMMINGS, Jr.,
Solicitor General.

FEBRUARY 1953.

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